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Budget Footnotes

A Newsletter of the Ohio Legislative Service Commission — January 2004

Fiscal Overview

— Allan Lundell

Most economic news for December was encouraging. The Federal Reserve's "Beige Book" reported continued improvement in the national economy, with most districts reporting that their economies "improved, strengthened, or grew at a moderate pace," but the Cleveland district reported a relatively unchanged economic environment with "slow and steady improvement in business conditions." The Bureau of Labor Statistics (BLS) reported that U.S. employment increased for the fifth consecutive month, but the increase of 1,000 was dramatically less than the consensus expectation of 127,000. In contrast to the BLS employment report, the "Beige Book" reported that most districts saw "modest improvements in labor markets in December." However, the Cleveland district reported "most firms still do not plan to increase payrolls in the near future." The national economy appears to be continuing its move into expansion, but Ohio is lagging behind.

For the fiscal year to date, total General Revenue Fund (GRF) revenue is $52 million (0.5%) below estimate. Total tax revenue is $26 million (0.3%) below estimate, but revenue from the major taxes is $17 million (0.2%) above estimate. Revenue from the "other" taxes, mostly the cigarette tax, the estate tax, and the foreign insurance tax, is $42 million (8.5%) below estimate. Through the first half of FY 2004, total GRF revenue is up 12.4% compared to FY 2003. The revenue growth is primarily due to the increase in the state sales tax rate and an increase in federal grants. If revenue from the sales tax and federal grants is subtracted from total GRF revenue, the resulting state-source revenue other than the sales tax is up just 1.5% compared to FY 2003.

Although December disbursements exceeded estimate by $32 million, fiscal year-to-date total GRF disbursements remain $335 million (2.6%) below estimate. Disbursements for primary and secondary education are $74 million (2.2%) below estimate and disbursements for higher education are $12 million (0.9%) below estimate. Disbursements for welfare and human services are $105 million (2.3%) below estimate. The only category of disbursements above estimate for the fiscal year is Other Transfers Out.

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Budget Footnotes examines the fiscal position of the state General Revenue Fund on a periodic basis.

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Table 1
General Revenue Fund
Simplified Cash Statement
($ in millions)

	Month of December	Fiscal Year 2004 to Date	Last Year	Difference
Beginning Cash Balance	-$793.9	$396.5		
Revenue + Transfers	$1,932.2	$11,095.0		
Available Resources	$1,138.4	$11,491.6		
Disbursements + Transfers	$1,978.8	$12,332.0		
Ending Cash Balances	-$840.4	-$840.4	-$1,403.2	$562.8
Encumbrances and Accts. Payable		$550.9	$640.4	-$89.5
Unobligated Balance		**-$1,391.3**	**-$2,043.7**	**$652.3**
BSF Balance		$180.7	$1,010.6	-$829.9
Combined GRF and BSF Balance		**-$1,210.6**	**-$1,033.1**	**-$177.5**

As shown in Table 1, the GRF began December with a negative cash balance of -$794 million. Revenue, including transfers-in, for December was $1,932 million. Disbursements, including transfers-out, were $1,979 million. The monthly deficit of $47 million thus brought the fiscal year-to-date cash balance to -$840 million. Although a negative cash balance may appear to be a cause for concern, the cash balance, due to the timing of revenues and disbursements, is generally negative early in the fiscal year before turning positive later in the year. If revenues and disbursements had met their estimates, the fiscal year-to-date cash balance would have been -$1,124 million, $284 million lower than the actual level. Chart 1 presents the monthly estimates of GRF revenues and disbursements for FY 2004 and the resulting month-end cash balances. Chart 2 compares actual month-end cash balances with the estimated month-end cash balances from Chart 1.

The fiscal year-to-date cash balance of -$840 million is $563 million higher (less negative) than a year ago. Year-to-date encumbrances of $551 million combine with the cash balance to yield an unobligated balance of -$1,391 million, which is $652 million higher than a year ago. Looking at just the unobligated balance indicates that the state's financial situation in terms of current-year performance, although not exceptional, has improved compared to a year ago. However, the $181 million balance in the Budget Stabilization Fund (BSF) is $830 million less than a year ago, and the combined GRF and BSF balance is $178 million lower than it was at this time last year. Thus, if one looks at the combined GRF and BSF balance, the state's financial situation in terms of ability to withstand an economic shock has deteriorated slightly from a year ago.

Chart 1: Estimated FY 2004, Revenues, Disbursements, and Month-end Cash Balances
(in millions of dollars)

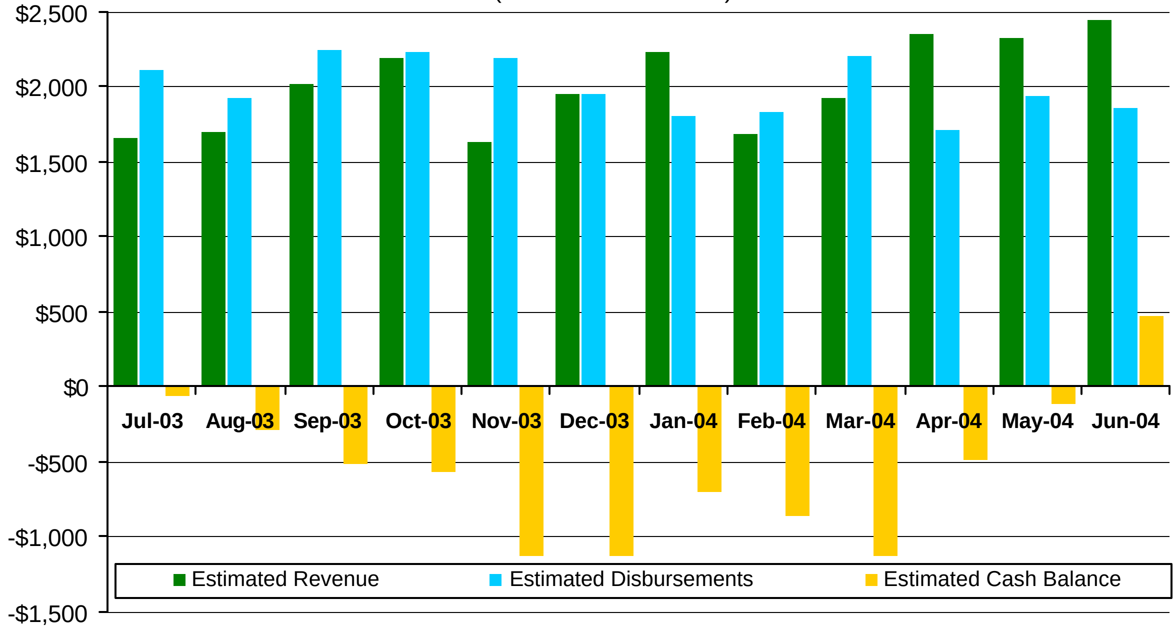
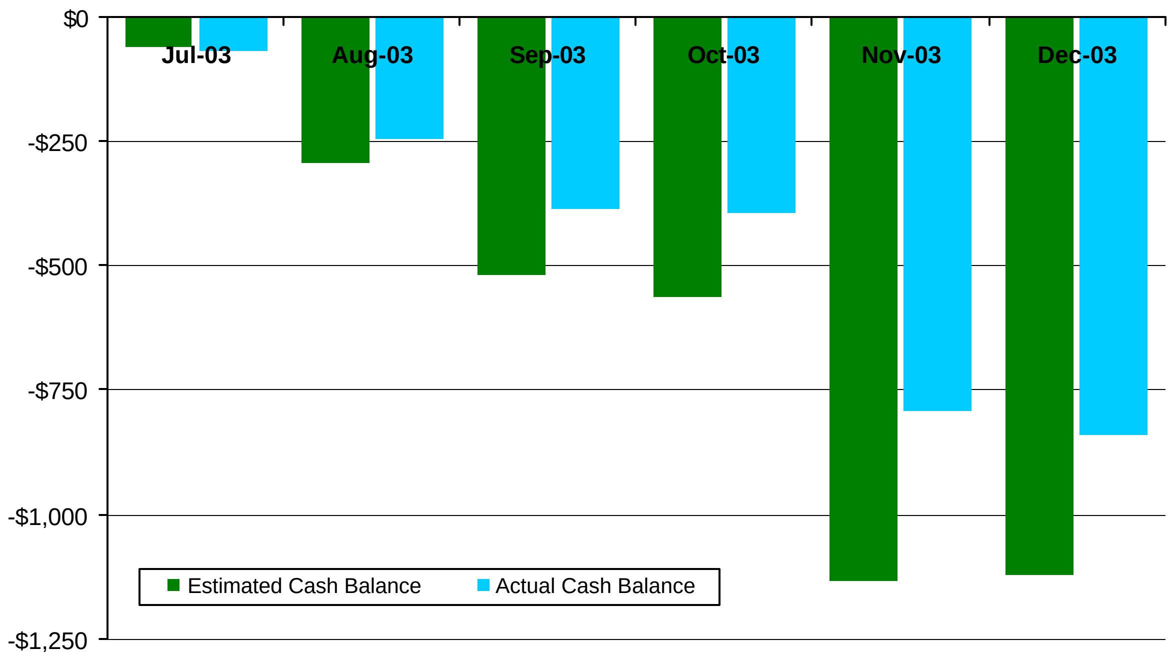


Chart 2: FY 2004 Month-end Cash Balances
(in millions of dollars)



TRACKING THE ECONOMY

¾ Phil Cummins

The mix of economic indicators in the past month included continued growth of industrial production in December and positive reports from purchasing managers. In contrast, total employment plateaued last month, and job gains since last summer were revised downward. Retail sales strengthened in December, but a jump in motor vehicle sales, stimulated by manufacturers' incentives, accounted for much of the rise. Continued economic expansion appears to be widely expected. Slow hiring raises concerns that the stimulus to consumer spending from the 2003 tax cuts and the surge of housing refinancings may run its course, and consumer spending growth may slow. Inflation at the finished goods and services level remained generally muted through year-end, as producers appear unable to pass along higher raw materials prices and instead rely on productivity enhancements to support profitability.

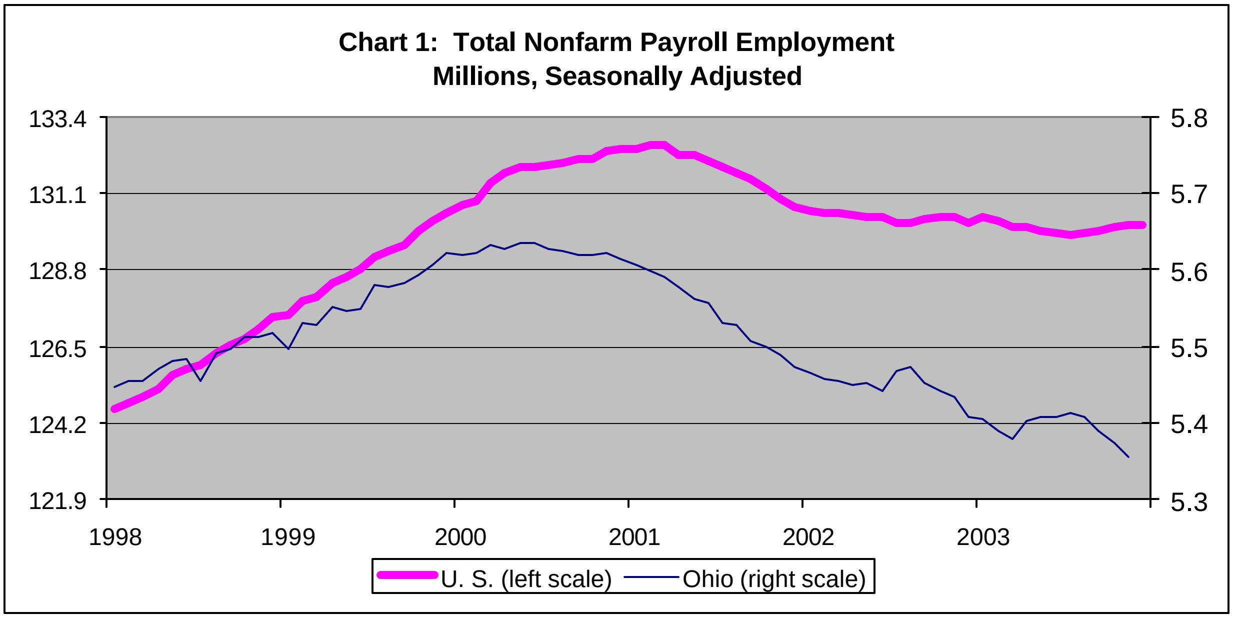
Recovery Continues but Is Stronger Elsewhere

Total nonfarm payroll employment nationwide was essentially unchanged in December, and revisions to October's and November's figures reduced the gains reported previously from the cyclical low in July. U.S. nonfarm payrolls rose a statistically insignificant 1,000 last month and were 280,000 higher than at the low point in July. Manufacturing employment fell again in December, as it has every month since August 2000, to its lowest level since 1958. In Ohio, total nonfarm payroll employment continued to drop through November (latest available), falling by 16,800 to the lowest level since early 1997. These trends in total employment are shown in Chart 1. Unemployment in the nation fell to 5.7% of the labor force in December, lowest since October 2002 and down from a peak of 6.3% in June. The unemployment rate in Ohio rose to 5.7% in November from 5.6% in October.

Purchasing managers at manufacturers nationwide reported growing production, orders, and order backlogs in December, in the Institute for Supply Management's monthly survey. The index for new orders was at its highest level (most widespread increases) since 1950. In contrast with the government's payroll employment report, which showed no significant growth, the purchasing managers said that factory employment rose in December for the second consecutive month. In a separate survey, purchasing managers with organizations other than manufacturers said that business activity, orders, order backlogs, and employment rose at their organizations in December.

Industrial production rose 0.1% in December, and manufacturing output rose 0.3%. Total factory production has been growing for the past two quarters and has risen nearly 4% since the recession low at the end of 2001, but it is still about 3% below the all-time peak in mid-2000. Output of consumer durables rose in December 2003 to its highest ever. Business equipment production has been growing strongly for the past two quarters, though it remains well short of levels reached in 2000. Output of construction supplies, also below its peak in 2000, has trended upward in the latest two quarters. Production of defense and space equipment has continued to trend upward, though not as rapidly as earlier. Industrial materials output rose in the latest two quarters.

Retail sales rose 0.5% in December to 6.7% above a year earlier. In part, the rise last month reflected strength in car and light truck sales, supported by factory incentives. Excluding December's 1.6% rise last month in sales of motor vehicles and parts, retail sales increased only 0.1%. Nevertheless, consumer spending contributed significantly to fourth-quarter GDP growth, even with a slowing in unit vehicle sales from exceptional levels last August.



Retailers with above-average gains in sales during the past year include building materials, furniture, appliances, electronics, and health and personal care stores. Sales of general merchandisers in December were 5.4% above a year earlier, reflecting strength at discounters and a 1.9% decline at department stores.

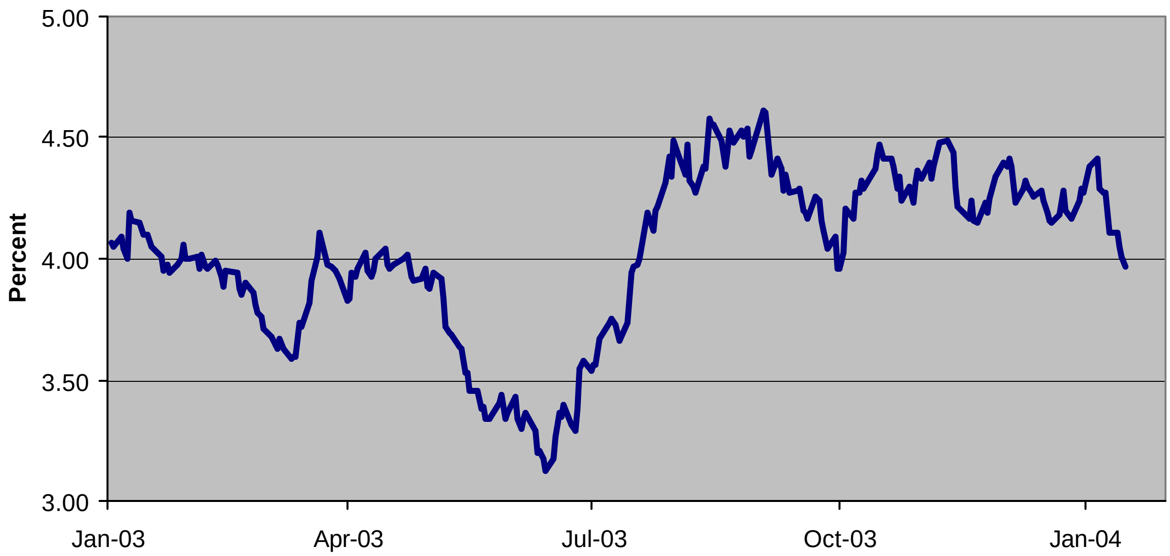
The "Beige Book," the Federal Reserve System's summary of information received from business contacts and others, continues to show improvement in the country's economy. Based on information gathered prior to January 6, the latest report indicates that the strongest region was the West Coast. Other regions were less upbeat, including the Cleveland Federal Reserve District, which includes Ohio. In this part of the country, business conditions continued to improve at the end of 2003, but only slowly. Manufacturing production was described as steady to slightly higher in recent months. Steel, industrial equipment, and truck and trailer manufacturers are seeing rising new orders and lengthening lead times. However, firms with rising demand appear to be relying mainly on overtime, rather than additions to staffing, to raise production, and some durable goods producers reportedly are planning workforce reductions. Retail sales were higher but short of expectations for many retailers, and were lower for department stores. Residential construction stayed strong in the region through year-end, but commercial builders saw little improvement.

Inflation Is Low for Finished Goods and Services

The producer price index for finished goods rose 0.3% in December reflecting a 1.8% rise in energy prices. Excluding energy, finished goods prices fell 0.1% last month. Compared with a year earlier, finished goods prices were 4% higher. Finished energy and food prices rose more rapidly, by nearly 12% and 8%, respectively. Smaller increases occurred in the aggregate for prices of other finished consumer goods and for capital equipment, each up only about 1% from December 2002. Increases in raw materials prices continue to be much larger than for most finished goods, as businesses apparently are unable in many cases to pass along these cost increases to their customers. The producer price index for crude materials rose 19% in the past year, reflecting sizable increases in prices of meat animals, soybeans, raw milk, cotton, metal scrap, crude oil, and natural gas.

Consumer prices rose 0.2% in December to 1.9% above a year earlier. As with producer prices, the rise in the consumer price index during the past year reflects, on average, more rapid increases in energy and food prices, and smaller increases in other prices. Some notable

Chart 2: 10-Year U.S. Treasury Interest Rate



exceptions to this generalization include prices for medical care services, up 4.2% in the past year, and education, up 7.2%. On the other hand, prices for personal computers and peripherals are estimated to have declined 18% in the year to December, and prices for telephone services fell 2.7%.

Interest Rates Decline

Credit market participants expected a more robust employment report for December and responded to the weaker-than-anticipated numbers by pushing interest rates down. Subsequent reports of mild inflation may have contributed to further interest rate declines. The ten-year Treasury bond yield dropped below 4% in mid-January, its lowest level since early October, as shown in Chart 2. Long-term interest rates were even lower in mid-2003 when Federal Reserve policy makers' public statements focused on the risk of deflation, and before employment began to recover. The Federal Reserve's target for federal funds remains at 1%, and policy makers are next scheduled to meet January 27.

Slow Ohio Population Growth

The U.S. Census Bureau recently released estimates of state populations as of July 1, 2003. Ohio's population on that date was estimated at 11,435,798. Ohio's population growth since July 1, 2002, at 0.2%, was third slowest among the states. The population of the United States rose 1.0% during this period. Only Massachusetts' population rose more slowly, and the number of people in North Dakota declined slightly, according to the Census Bureau estimates. The other states among the ten slowest growing states were Iowa, New York, Pennsylvania, West Virginia, Michigan, Kansas, and Vermont. Slow growth of Ohio's population reflects a combination of factors. The rate of natural increase – births minus deaths, divided by population on July 1, 2002 – was 15th lowest among the states at 0.3%. The rate of natural increase for the country as a whole was 0.5%. Ohio was one of 20 states from which more people migrated to other states than moved from other states. Only 9 of these states lost population more rapidly, as a percentage of year-earlier population. Finally, the increase in Ohio's population from net international migration was relatively small. Migration rates, within the country and internationally, were plausibly driven primarily by job opportunities, though other factors such as retirement and climate preferences also influence migration.

Status of the General Revenue Fund

REVENUE

— *Allan Lundell, Jean Botomogno, Ross Miller, and Ruhaiza Ridzwan*

Encouraging revenue news continued in December. Revenue from the personal income tax exceeded estimate for the second straight month and is now above estimate for the fiscal year. Revenue from the sales tax was slightly below estimate in December but is on target with estimate for the fiscal year to date. Revenues from the cigarette tax and the estate tax, which were mentioned last month as sources of discouraging revenue news, exceeded estimates. Although December GRF revenues of $1,932.2 million were $22.9 million (1.2%) below estimate, GRF revenue less federal grants (state-source revenue) was $16.0 million (1.1%) above estimate. Revenue from federal grants was $38.9 million (8.0%) below estimate in December, but this may be related to December Medicaid disbursements being $62.4 million (7.7%) below estimate. Total tax revenue was $24.3 million (1.7%) above estimate and revenue from the major taxes was $13.4 million (1.0%) above estimate.[1]

Through the first half of FY 2004, GRF revenue is up 12.4% compared to FY 2003. State-source revenue is up 9.7% and revenue from federal grants is up 20.8%. Federal grants are up partly due to one-time revenue. Total tax revenue is up 10.2% and revenue from the major taxes is up 11.9%. Total GRF revenue is up $1,221.4 million compared to FY 2003, but most of the increase (94%) is from the sales tax (up $664.2 million) and federal grants (up $488.9 million). State-source revenue other than the sales tax is up just $68.3 million (1.5%) compared to FY 2003, reflecting slow growth in the Ohio economy.

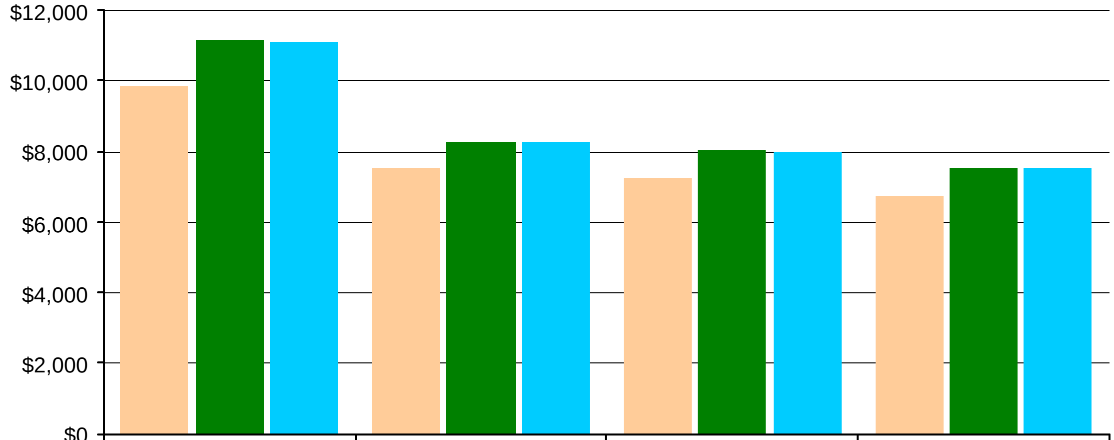
Although revenues are up compared to FY 2003, they remain slightly below FY 2004 estimates. Total GRF revenue is $51.5 million (0.5%) below estimate through the first six months of this fiscal year. State-source revenue is $15.6 million (0.2%) below estimate, and total tax revenue is $25.6 million (0.3%) below estimate. Revenue from the major taxes, which are expected to account for 69% of total GRF revenue and 89% of state-source revenue for the fiscal year, is $16.6 million (0.2%) above estimate. The recovery in revenue from the major taxes provides encouragement heading into the second half of FY 2004. Chart 1 compares FY 2004 revenues with FY 2003 revenues and FY 2004 estimates.

Personal Income Tax

December was the second straight month in which personal income tax receipts exceeded estimate. The GRF received $681.4 million in revenue from the personal income tax. This amount was $27.1 million (4.1%) above estimate. The $637.4 million in revenue collected through withholding was $22.8 million (3.5%) below estimate. Withholding reflects the condition of Ohio's labor market and will not strengthen until the labor market strengthens and employment increases. Quarterly estimated payments of $105.9 million were $35.9 million (51.3%) above estimate.[2] Refunds totaled $9.6 million. This total was $10.4 million (51.9%) less than estimate.

Through the first half of FY 2004, GRF revenue from the personal income tax totals $3,542.3 million. The total is $16.9 million (0.5%) above estimate. Withholding is $17.8 million (0.5%) below estimate. Quarterly estimated payments are $35.3 million (9.5%) above estimate, revenue from the tax on trusts is $6.4 million (40.9%) below estimate, and refunds are $12.9 million (7.8%)

Chart 1: Year-to-Date GRF Revenue
(in millions of dollars)



	Total GRF Revenue	Total GRF Revenue less Federal Grants	Revenues from Total Taxes	Revenues from Major Taxes
FY 2003	$9,873.7	$7,522.6	$7,260.8	$6,743.9
FY 2004 Estimate	$11,146.6	$8,270.7	$8,025.9	$7,532.4
FY 2004 Actual	$11,095.0	$8,255.1	$8,000.3	$7,549.0

below estimate. The income tax is showing slight growth compared to a year ago. GRF revenue from the personal income tax is up by 2.3%. Gross collections are up by 2.0% and withholding is up by 2.3%. Quarterly estimated payments are up by 4.3% and refunds are down by 1.4%.

Sales and Use Tax

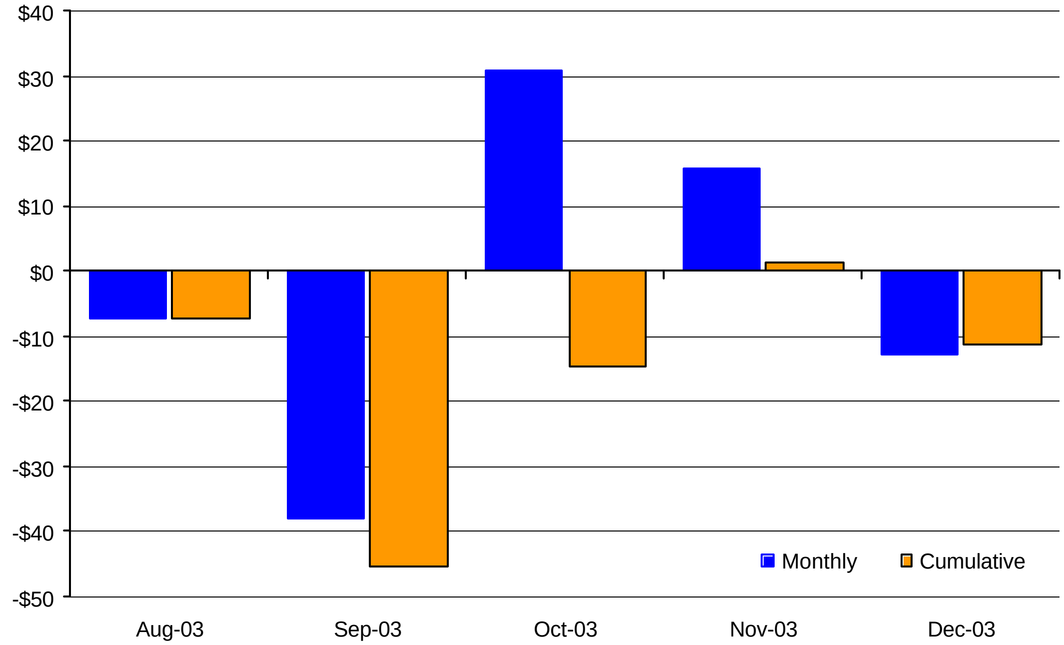
In December 2003, revenues from the auto sales tax exceeded estimates, while those from the nonauto sales and use tax lagged estimates. Total sales and use tax revenues in the month were $676.5 million, $1.8 million (0.3%) below estimates. Total receipts were $193.5 million (40.1%) above December 2002 sales and use tax revenues. As of December 2003, year-to-date total sales and use tax revenues were $3,739.0 million, tracking year-to-date estimates. Sales and use tax receipts were $664.2 million (21.6%) higher than year-to-date tax receipts in December 2002. Most of the increase in revenue is due to a 20% increase in tax rates as the tax increased from 5% to 6% of the purchase price in July 2003.

Nonauto Sales and Use Tax

The nonauto sales and use tax was below estimates this month, after exceeding estimates in the prior two months. This tax source provided $584.9 million in December 2003, $12.7 million (2.1%) below estimates. Tax receipts partly reflect taxable retail sales activity in the prior month and also taxable retail sales during that month.[3] Compared to nonauto sales tax revenues a year ago, tax receipts for the month were $169.8 million (40.9%) higher than revenues in December 2002. Revenue growth in December was high due to a difference in tax collection patterns between this year and last year. H.B. 40 caused some December sales to be included in December revenue while last year December revenue was due only to November sales. (More detail on H.B. 40 is provided later in this article.)

As of December 2003, year-to-date nonauto sales and use tax receipts were $3,160.4 million, $11.4 million (0.4%) below estimates, due to the weak December performance. Compared to receipts a year ago, year-to-date nonauto sales tax receipts as of December 2003 increased $569.1 million (22.0%). The performance of the nonauto sales and use tax in December reversed the cumulative variance from positive into negative territory. In November 2003, the year-to-date variance turned positive by $1.3 million. In December 2003, nonauto sales

Chart 2: Nonauto Sales Tax Variance from July 2003 Estimates
(in millions of dollars)



and use tax revenues were short of estimates by $12.7 million, and the year-to-date variance fell to $11.4 million below estimates.

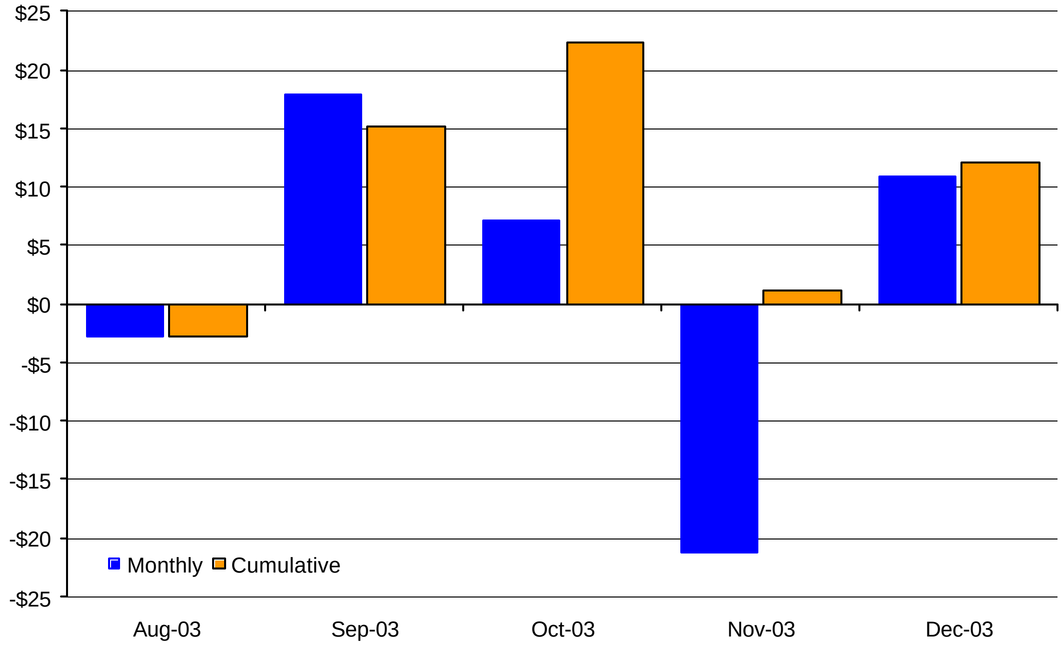
In the last three months, the growth in nationwide retail sales (excluding autos) has been positive, but modest. Growth in retail sales in October and November 2003 were 0.4% and 0.7%, respectively. December retail sales growth (excluding autos) came in at a weak 0.1%, below expectations. Comparisons with previous-year retail sales are solid, but not spectacular. Compared to the same months in CY 2002, nationwide retail sales (excluding autos) were up 6.5% in October 2003, 6.9% in November 2003, and 6.7% in December 2003. The Total Retail Chain Store Index of the International Council of Shopping Centers reported year-over-year growth of 8.4%, 8.8%, and 9.2% in October 2003, November 2003, and December 2003, respectively.[4]

Auto Sales Tax

Auto sales tax receipts were $91.7 million in December 2003, $10.8 million (13.4%) above estimates. The surge in receipts was in part due to the recording of some of November auto sales at the beginning of December 2003 (the same timing issue depressed November receipts) and in part to strong sales during the month. Auto tax payments are made by the clerks of court on Monday for taxes collected during the preceding week on motor vehicles, watercraft, and outboard motors titled. Therefore, auto tax receipts largely reflect vehicles sold and titled during the month. Compared to revenues a year ago in the same month, auto sales tax receipts in December 2003 were $23.8 million (35.0%) higher than receipts in FY 2003.[5] As of December 2003, year-to-date auto sales tax receipts were $578.6 million, $12.0 million (2.1%) above estimates. These receipts were also $95.1 million (19.7%) higher than receipts through the same period in December 2002.

Nationwide auto sales, both in number of vehicles sold and dollar sales, were strong in December 2003.[6] The U.S. Department of Commerce reported that sales at motor vehicle dealers grew 1.6% in December 2003. Light vehicle unit sales surged to 18.0 million vehicles in December 2003 on an annualized basis, up from 16.8 million in November, buoyed by the traditional end of calendar year discounting by automakers and hefty incentives.[7] Manufacturers sold 16.7 million light vehicles in CY 2003, slightly less than the total of 16.8 million in CY 2002. Low

Chart 3: Auto Sales Tax Variance from July 2003 Estimate
(in millions of dollars)



interest rate financing and the lengthening of loan periods, which bring down the monthly payments, continue to support the affordability of vehicle sales.

Estimated Taxable Sales in FY 2004

The table below shows year-to-date estimated taxable sales in FY 2004 and a comparison with taxable sales in the same period in FY 2003. The sales and use tax rate was increased to 6% on July 1, 2003, up from 5%. Taxable sales were estimated by dividing sales tax receipts by the corresponding tax rate. The table illustrates, based on actual tax receipts, an estimate of the growth in the sales and use tax base. It shows that the underlying sales and use tax taxable base in the first half of FY 2004 grew 1.3% from the first half of FY 2003. Nonauto taxable sales grew 1.6%, while auto taxable sales declined 0.3%. Information in the table must be used with caution because it ignores the effect of H.B. 40, which modified sales and use tax collections. Also, it does not take into account the probable acceleration of purchases of big-ticket items (e.g., cars, furniture, appliances, etc.) in June 2003 ahead of the rate increase that occurred on July 1, 2003. This effect was most likely larger for the auto sales tax than for the nonauto sales tax. Based on research from the Department of Taxation, between $20 and $40 million in potential FY 2004 auto tax revenues were transferred due to the shifting of purchases of automobiles into FY 2003.

Estimated Taxable Sales (based on tax collections), in millions			
	Auto Sales Tax	Nonauto Sales Tax	Total
FY 2003	$9,669.8	$51,826.2	$61,495.9
FY 2004	$9,642.8	$52,673.0	$62,315.8
Growth	-0.3%	1.6%	1.3%

Due to H.B. 40, remitters of nonauto sales and use tax payments whose liability is large enough to require payment via electronic funds transfers (EFT) have to remit about 70% of the liability accrued in any given month in that same month, rather than 100% of the liability in the following month when the return is filed (prior to H.B. 40). For example, some portion of the December 2003 nonauto sales and use tax collections is based on November 2003 sales activity, with sales tax returns filed in December 2003. The other portion of December 2003 tax collections (the accelerated payments portion) is based on December 2003 sales activity. Electronic benefit transfer tax payment remitters that were affected by H.B. 40 remit about 78% to 80% of the nonauto sales and use tax payments. The H.B. 40 changes will render problematic any comparison of year-to-year nonauto sales and use tax collections, at least until April 2004. However, it is reasonable to believe that actual growth in the nonauto portion of the tax base in the first half of FY 2004 was probably less than 1.6%. Therefore, the nonauto sales and use tax as a revenue source appears to be weak and is still struggling to generate upside momentum.

Corporate Franchise Tax

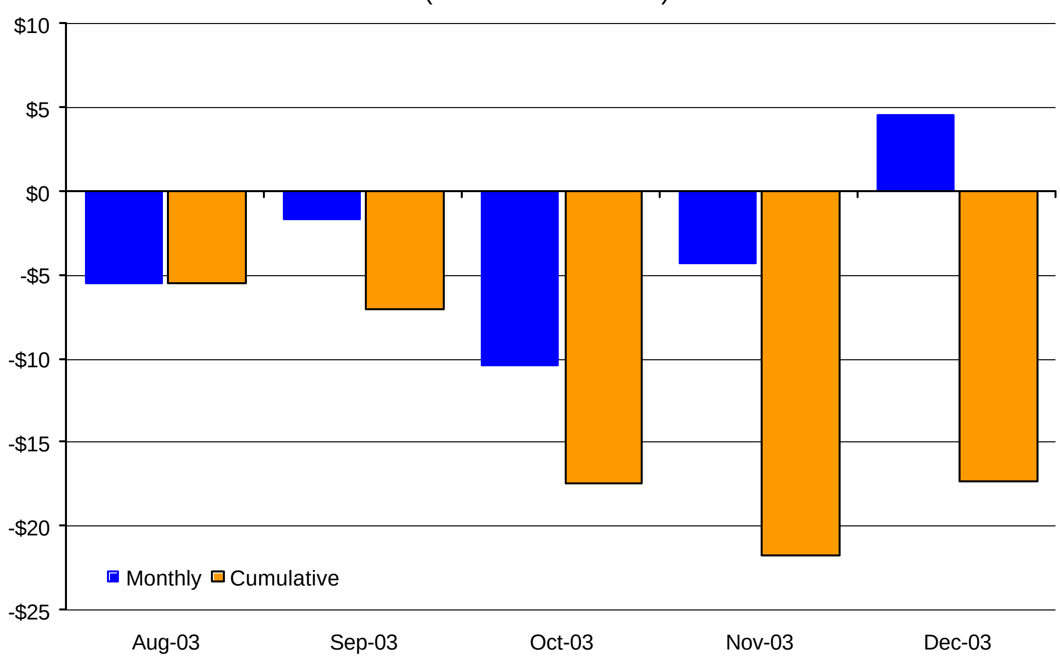
Activities under the franchise tax in the first half of the fiscal year are generally refunds, tax payments due to audit findings, late payments, and other tax reconciliations. Major tax receipts under this tax are due in the second half of the fiscal year, with the first major tax payment due in January 2004. Corporate franchise tax refunds were higher than receipts by $22.9 million in December 2003. As of December 2003, year-to-date revenue is $16.8 million, $14.9 million above estimates. Corporate franchise tax revenues were $56.4 million greater than receipts in the same period last year (which were -$39.6 million, indicating that refunds were greater than receipts). The corporate franchise tax is expected to continue to improve in FY 2004. The Office of Budget and Management estimates that FY 2004 corporate franchise tax revenues will be $793.0 million, up from $747.3 million in FY 2003 and $721.3 million in FY 2002. With revenues $56.4 million higher than last year, the tax is well positioned for good results the remainder of the fiscal year.

Cigarette and Other Tobacco Products Tax

Cigarette and other tobacco products tax receipts were above estimates for the first time this fiscal year. Receipts in December 2003 were $52.1 million, $4.5 million (9.4%) above estimates. Revenues from this tax source were $0.7 million (1.3%) lower than receipts in December 2002.

As of December 2003, year-to-date cigarette and other tobacco products receipts were $254.3 million, $17.3 million (6.4%) below estimates. As of December 2003, year-to-date revenues from this tax source were $41.2 million (14.0%) below revenues a year ago. Receipts from the floor tax in FY 2003 and the change in the bonding requirements for cigarette dealers resulting from Am. Sub. H.B. 95 (the biennial appropriations act) skew

Chart 4: Cigarette Tax Variance from July 2003 Estimates
(in millions of dollars)



comparisons of actual tax revenues in FY 2004 with current year estimates, and also with year ago receipts. In the first half of FY 2003, the floor tax[8] provided $31.7 million. Excluding amounts provided by the floor tax, year-to-date FY 2004 revenues as of December 2003 would have been $9.5 million (3.6%) below receipts in the same period in FY 2003.

H.B. 95 changed how certain dealers acquire stamps or tax indicia to affix to their products. Prior to H.B. 95, cigarette and other tobacco dealers had to pay cash for the stamps or post bond against the stamps they received. This is essentially how these taxpayers paid state or county cigarette taxes. Due to H.B. 95, certain taxpayers in "good standing" are now able to receive stamps on credit and make payment of their tax liability when tax returns are filed. The change decreased cigarette tax receipts, most noticeably in October 2003. This timing issue will reverse during the fiscal year, most likely in May 2004, when tax reconciliations for the fiscal year are made for the cigarette and other tobacco products tax.

As of December 2003, stamp sales (cash and on credit) were approximately $280 million, based on data provided by the Department of Taxation, yet cigarette and tobacco products tax receipts were only $254.3 million. Estimates for this tax source were for about $272 million, which is less than the amount of stamps sold. Thus, when taking into account the effect of the change in stamp purchases this year, which created a temporary revenue loss, the "true" negative variance from estimates as of December 2003, if any, may be small. Also, when taking into account both the change in stamp purchases and the floor tax revenues in FY 2003, the comparison with year-ago receipts does not appear as severe as calculated above.

Kilowatt-hour Excise Tax

Revenues from the kilowatt-hour excise tax for the first half of FY 2004 are below estimate by $19.0 million, or just over 10%. In fact revenues have fallen as compared with FY 2003, with revenues 2.6% below the level for the first half of the fiscal year just past. The revenue shortfall as compared with last year is due in part to a mild summer, which allowed households to reduce electricity usage for air conditioning, and possibly in part to continuing weakness in the economy restraining commercial and industrial usage. When comparing with the FY 2004 estimate, this shortfall is apparently compounded by a problem associated with calculating the effect of the local government fund freeze on the GRF. LSC economists expect the current trend to continue, with revenues for the full fiscal year approximately 10 percent below the estimate, barring any unforeseen weather or economic developments. An OBM official confirms that revenues from this tax are not expected to recover sufficiently during the next six months to reach the estimate for the full fiscal year.

Estimated revenues for the first half of the fiscal year were 8.4% higher than actual revenues for the first half of FY 2003; for the full fiscal year, revenues are estimated to grow by 9.7% compared with FY 2003. Both growth rates are significantly higher than the long-run trend rate of growth in electricity usage, 1.8%, projected by the federal Energy Information Administration in *Annual Energy Outlook 2004 (Early Release).* Since FY 2003 revenues were over 5% greater than FY 2002 revenues, there is little reason to anticipate that electricity usage, and therefore revenue from the tax, will grow substantially faster than the long-run trend rate. Furthermore there were no changes to the tax that would increase revenues.

The growth rate may have been overestimated due to an incorrect treatment of the local government fund freeze. Under statute, the local government funds are supposed to receive 3.024% of the revenue from this tax. That amount has gone instead to the GRF since FY 2002 because of the freezes contained in Am. Sub. H.B. 94 of the 124th General Assembly and Am. Sub. H.B. 95 of the 125th General Assembly.[9] The estimated revenue under this tax may have doublecounted the share of the revenue that would have gone to the local government funds under the statutory formula (but that goes to the GRF under the local government fund freeze).

Public Utility Excise Tax

Public utility excise tax revenues for the first half of FY 2004 are $3.3 million (4.1%) above estimate. It is likely that revenues from this tax will end the year above estimate. This is due almost entirely to collections from natural gas companies. Revenues collected from such companies during the first half of the year are just over 40% higher than during the first half of FY 2003, primarily due to higher prices for natural gas.[10] This performance is partially offset by a fall of just over 20% in revenues collected from local telephone companies. That fall was mostly due to larger refunds being given in November 2003 (a total of $8.7 million) than were given in November 2002 ($2.1 million). Under this tax, telephone companies make advance payments that are based on their previous year's tax liability, and refunds are given in November if total advance payments exceed the actual tax liability.

Estate Tax

Although December estate tax revenue was $9.8 million (210.8%) greater than estimated, fiscal year-to-date estate tax revenue of $37.2 million is below estimate by $15.3 million (29.2%). The estate tax is one of the more volatile state revenue sources, as the estate of a very wealthy individual can account for 10% or more of the total state estate tax revenues. An estate's tax liability depends on the estate's value at the time a person dies and the time at which a settlement is made by each county to the state. The bearish stock market of recent years, low interest rates, and the phase-in effect of the changes in estate tax valuations and credits in S.B. 108 of the 123rd General Assembly are several other factors that affected estate tax revenue collections in the first half of FY 2004. Taking into consideration the poor stock market performance in the last three years and lower interest rates, it is possible that estate tax revenue for FY 2004 will be lower than the estimate of $105.2 million.

Earnings on Investments

Through the first half of FY 2004, accumulated state earnings on investments of $14.8 million are $1.5 million (11.5%) greater than estimated. State portfolio performance in the last six months has been consistent with the estimates. Factors contributing to this performance were stable GRF balances and higher interest rates than last year. In the second half of FY 2004, interest rates are expected to be higher than in the previous year. Therefore, earnings on investments have a good chance of meeting the FY 2004 estimate of $25 million.

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[1] The "major taxes" are the personal income tax, the sales and use tax, the corporate franchise tax, the public utility excise tax, and the kilowatt-hour tax.

[2] Quarterly estimated payments are made by taxpayers who expect to be underwithheld by more than $500. Payments are due on or before April 15, June 15, and September 15 of the tax year and January 15 of the following year. These payments are usually made by taxpayers with significant nonwage income. This income often comes from investments, especially capital gains realized in the stock market. Most estimated payments are made by high-income taxpayers.

[3] Am. Sub. H.B. 40 changed the historical patterns of remittance of sales and use tax receipts. Under prior law, monthly sales and use tax receipts reflected taxable transactions in the prior month. Under current law, certain large taxpayers must remit sales tax payments in the same month the transactions occur. Thus, monthly sales tax receipts reflect taxable transactions in both the current and the prior month.

(Endnotes, continued)

[4] The International Council of Shopping Centers' Total Retail Chain Store Index measures sales at about 80 major retailers. Sales are from all stores, including sales from store expansions, relocations, and mergers.

[5] At the 5% rate, December auto sales tax revenue would have been about $76.4 million, $8.5 million more than FY 2003 receipts in the same month.

[6] Annualized sales of vehicles and light trucks were 18.9 million in August 2003, 16.6 million in September 2003, 15.5 million in October 2003, and 16.8 million units in November 2003.

[7] According to CNW Marketing/Research, among the major automakers, General Motors' average incentive was $4,395. Ford and Chrysler incentives were $4,271 and $4,394, respectively. Toyota and Honda's incentives were lower, $2,766 and $1,371, respectively.

[8] The "floor" tax is the additional tax paid by dealers on cigarettes in inventory when the tax rate was increased from 22 cents to 55 cents on July 1, 2003.

[9] Viewing all utility-related taxes as a whole, the local government funds were not penalized, since the amount they received under the public utility excise tax was based on revenue amounts received when electric companies were still subject to that tax.

[10] Residential gas prices in Ohio reported by the federal Energy Information Administration for August 2003, the most recent month available, were over 13% higher than the figure reported for the previous year. For commercial and industrial customers the increases were 25% and 51%, respectively.

Table 2
General Revenue Fund Income
Actual vs. Estimate
Month of December 2003
($ in thousands)

REVENUE SOURCE				
TAX REVENUE	**Actual**	**Estimate***	**Variance**	**Percent**
Auto Sales	$91,667	$80,819	$10,848	13.4%
Non-Auto Sales & Use	$584,880	$597,577	-$12,697	-2.1%
Total Sales	$676,547	$678,396	-$1,849	-0.3%
Personal Income	$681,385	$654,276	$27,109	4.1%
Corporate Franchise	-$22,928	-$15,860	-$7,068	44.6%
Public Utility	-$1,335	$300	-$1,635	-545.2%
Kilowatt Hour Excise Tax	$24,825	$27,968	-$3,143	-11.2%
Total Major Taxes	**$1,358,493**	**$1,345,080**	**$13,413**	**1.0%**
Foreign Insurance	$36	$0	$36	---
Domestic Insurance	$0	$0	$0	---
Business & Property	$89	$155	-$66	-42.4%
Cigarette	$52,085	$47,600	$4,485	9.4%
Alcoholic Beverage	$4,850	$4,920	-$70	-1.4%
Liquor Gallonage	$2,492	$2,580	-$88	-3.4%
Estate	$9,789	$3,150	$6,639	210.8%
Total Other Taxes	$69,341	$58,405	$10,936	18.7%
Total Taxes	**$1,427,834**	**$1,403,485**	**$24,349**	**1.7%**
NON-TAX REVENUE				
Earnings on Investments	$6,703	$6,250	$453	7.3%
Licenses and Fees	$638	$1,323	-$685	-51.8%
Other Revenue	$32,220	$39,000	-$6,780	-17.4%
Non-Tax Receipts	$39,561	$46,573	-$7,012	-15.1%
TRANSFERS				
Liquor Transfers	$16,000	$15,000	$1,000	6.7%
Budget Stabilization	$0	$0	$0	---
Other Transfers In	$1,802	$4,100	-$2,298	-56.0%
Total Transfers In	$17,802	$19,100	-$1,298	-6.8%
TOTAL REVENUE less Federal Grants	**$1,485,198**	**$1,469,158**	**$16,040**	**1.1%**
Federal Grants	$447,029	$485,970	-$38,941	-8.0%
TOTAL GRF REVENUE	**$1,932,227**	**$1,955,128**	**-$22,901**	**-1.2%**

* August 2003 estimates of the Office of Budget and Management.

Detail may not sum to total due to rounding.

Table 3
General Revenue Fund Income
Actual vs. Estimate
FY 2004 to Date as of December 2003
($ in thousands)

REVENUE SOURCE						Percent
TAX REVENUE	**Actual**	**Estimate***	**Variance**	**Percent**	**FY 2003**	**Change**
Auto Sales	$578,595	$566,555	$12,040	2.1%	$483,475	19.7%
Non-Auto Sales & Use	$3,160,376	$3,171,759	-$11,383	-0.4%	$2,591,300	22.0%
Total Sales	$3,738,971	$3,738,314	$657	0.0%	$3,074,775	21.6%
Personal Income	$3,542,283	$3,525,419	$16,864	0.5%	$3,461,940	2.3%
Corporate Franchise	$16,782	$1,983	$14,799	746.3%	-$39,562	-142.4%
Public Utility	$82,935	$79,677	$3,258	4.1%	$74,223	11.7%
Kilowatt Hour Excise Tax	$167,995	$186,972	-$18,977	-10.1%	$172,538	-2.6%
Total Major Taxes	**$7,548,966**	**$7,532,365**	**$16,601**	**0.2%**	**$6,743,914**	**11.9%**
Foreign Insurance	$114,737	$122,566	-$7,829	-6.4%	$115,365	-0.5%
Domestic Insurance	$147	$200	-$53	-26.3%	$1,626	-90.9%
Business & Property	$1,254	$1,521	-$267	-17.5%	$1,081	16.0%
Cigarette	$254,265	$271,619	-$17,354	-6.4%	$295,497	-14.0%
Alcoholic Beverage	$28,541	$30,268	-$1,727	-5.7%	$28,714	-0.6%
Liquor Gallonage	$15,224	$14,814	$410	2.8%	$14,677	3.7%
Estate	$37,164	$52,500	-$15,336	-29.2%	$59,930	-38.0%
Total Other Taxes	$451,331	$493,488	-$42,157	-8.5%	$516,890	-12.7%
Total Taxes	**$8,000,297**	**$8,025,853**	**-$25,556**	**-0.3%**	**$7,260,804**	**10.2%**
NON-TAX REVENUE						
Earnings on Investments	$14,768	$13,250	$1,518	11.5%	$22,810	-35.3%
Licenses and Fees	$16,187	$18,915	-$2,728	-14.4%	$13,246	22.2%
Other Revenue	$86,163	$94,231	-$8,068	-8.6%	$114,374	-24.7%
Non-Tax Receipts	$117,119	$126,396	-$9,277	-7.3%	$150,430	-22.1%
TRANSFERS						
Liquor Transfers	$62,000	$56,000	$6,000	10.7%	$61,000	1.6%
Budget Stabilization	$0	$0	$0	---	$0	---
Other Transfers In	$75,681	$62,462	$13,219	21.2%	$50,412	50.1%
Total Transfers In	$137,681	$118,462	$19,219	16.2%	$111,412	23.6%
TOTAL REVENUE less Federal Grants	**$8,255,097**	**$8,270,711**	**-$15,614**	**-0.2%**	**$7,522,647**	**9.7%**
Federal Grants	$2,839,942	$2,875,842	-$35,900	-1.2%	$2,351,012	20.8%
TOTAL GRF REVENUE	**$11,095,039**	**$11,146,553**	**-$51,514**	**-0.5%**	**$9,873,659**	**12.4%**

* August 2003 estimates of the Office of Budget and Management.

Detail may not sum to total due to rounding.

DISBURSEMENTS

— *Steve Mansfield**

At the halfway point of the fiscal year, General Revenue Fund (GRF) disbursements (excluding transfers) stand at $346.2 million below estimate. December's disbursements reduced the overall negative disbursement variance with a net positive disbursement variance of $30.2 million. Of the state's four major GRF program categories, the Welfare and Human Services category is below the year-to-date estimate by $176.5 million (having added in December $53.3 million in spending below estimate), with the Education and Government Operations categories also posting significant negative disbursement variances for the year to date (see Figure 1). In order of magnitude, the three largest program subcategories contributing to the year-to-date negative disbursement variance are Health Care/Medicaid (-$104.6 million), Primary and Secondary Education (-$73.6 million), and Justice and Corrections (-$56.6 million). In December, the Tax Relief program posted a significant positive disbursement variance, virtually erasing its negative variances from the previous two months. As can be seen in Table 5, all program subcategories are posting negative year-to-date disbursement variances.

In the sections that follow, we examine in more detail the disbursement activity in each of the four major GRF program categories in the order of magnitude of its contribution to the year-to-date negative disbursement variance. Summary information about GRF disbursement activity for the most recent month is presented in Table 4, and for the year to date is presented in Table 5. A detailed analysis of disbursement activity in the Health Care/Medicaid program is presented in Tables 6 and 7.

Welfare/Human Services (-$176.5 million)

The Welfare/Human Services category posted a negative disbursement variance of $53.3 million in December to stand at $176.5 million below the estimate for the year to date. The Health Care/Medicaid subcategory now accounts for the largest part of the category's year-to-date negative variance. The following paragraphs discuss the disbursements in the components of the Welfare/Human Services category in more detail.

Figure 1
GRF Disbursement Variances
by Program Category, FY 2004

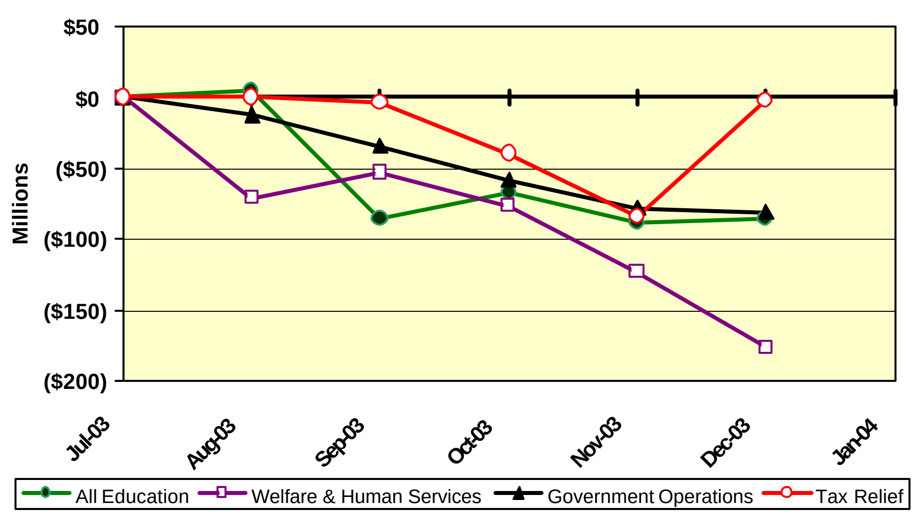

Table 4
General Revenue Fund Disbursements
Actual vs. Estimate
Month of December 2003
($ in thousands)

USE OF FUNDS

PROGRAM	**Actual**	**Estimate***	**Variance**	**Percent**
Primary & Secondary Education (1)	$515,320	$505,931	$9,389	1.9%
Higher Education	$165,621	$171,611	-$5,990	-3.5%
Total Education	$680,941	$677,543	$3,399	0.5%
Health Care/Medicaid	$746,450	$808,837	-$62,387	-7.7%
TANF	$50,869	$63,532	-$12,663	-19.9%
General/Disability Assistance	$1,622	$1,881	-$259	-13.8%
Other Welfare (2)	$45,265	$49,794	-$4,529	-9.1%
Human Services (3)	$89,912	$63,356	$26,556	41.9%
Total Welfare & Human Services	$934,118	$987,400	-$53,282	-5.4%
Justice & Corrections	$126,379	$128,632	-$2,253	-1.8%
Environment & Natural Resources	$5,671	$7,367	-$1,696	-23.0%
Transportation	$1,527	$2,377	-$850	-35.8%
Development	$8,650	$8,944	-$294	-3.3%
Other Government	$25,838	$22,708	$3,130	13.8%
Capital	$0	$412	-$412	-100.0%
Total Government Operations	$168,065	$170,440	-$2,375	-1.4%
Property Tax Relief (4)	$183,354	$101,000	$82,354	81.5%
Debt Service	$10,639	$10,549	$91	0.9%
Total Program Payments	**$1,977,117**	**$1,946,932**	**$30,186**	**1.6%**
TRANSFERS				
Local Govt Distribution	$0	$0	$0	---
Budget Stabilization	$0	$0	$0	---
Other Transfers Out	$1,639	$0	$1,639	---
Total Transfers Out	$1,639	$0	$1,639	---
TOTAL GRF USES	**$1,978,757**	**$1,946,932**	**$31,825**	**1.6%**

(1) Includes Primary, Secondary, and Other Education.
(2) Includes the Department of Job and Family Services, exclusive of Medicaid, TANF, and General/Disability Assistance.
(3) Includes Mental Health, Mental Retardation and Developmental Disabilities, and Other Human Services.
(4) Includes property tax rollbacks, homestead exemption, and tangible property tax exemption.

* August 2003 estimates of the Office of Budget and Management.

Detail may not sum to total due to rounding.

Table 5
General Revenue Fund Disbursements
Actual vs. Estimate
FY 2004 to Date as of December 2003
($ in thousands)

USE OF FUNDS

PROGRAM	**Actual**	**Estimate***	**Variance**	**Percent**	**FY 2003**	**Percent Change**
Primary & Secondary Education (1)	$3,233,079	$3,306,706	-$73,627	-2.2%	$3,253,339	-0.6%
Higher Education	$1,241,996	$1,253,771	-$11,775	-0.9%	$1,245,207	-0.3%
Total Education	$4,475,075	$4,560,477	-$85,402	-1.9%	$4,498,546	-0.5%
Health Care/Medicaid	$4,493,537	$4,598,136	-$104,599	-2.3%	$4,133,036	8.7%
TANF	$227,007	$239,399	-$12,392	-5.2%	$280,465	-19.1%
General/Disability Assistance	$11,954	$13,060	-$1,105	-8.5%	$13,956	-14.3%
Other Welfare (2)	$282,062	$322,776	-$40,713	-12.6%	$278,937	1.1%
Human Services (3)	$613,774	$631,436	-$17,662	-2.8%	$670,121	-8.4%
Total Welfare & Human Services	$5,628,335	$5,804,806	-$176,472	-3.0%	$5,376,515	4.7%
Justice & Corrections	$956,940	$1,013,575	-$56,635	-5.6%	$952,603	0.5%
Environment & Natural Resources	$67,600	$69,468	-$1,868	-2.7%	$78,298	-13.7%
Transportation	$13,745	$16,517	-$2,772	-16.8%	$18,930	-27.4%
Development	$81,170	$90,974	-$9,804	-10.8%	$110,705	-26.7%
Other Government	$217,017	$225,031	-$8,015	-3.6%	$224,521	-3.3%
Capital	$0	$1,740	-$1,740	-100.0%	$0	---
Total Government Operations	$1,336,472	$1,417,305	-$80,833	-5.7%	$1,385,056	-3.5%
Property Tax Relief (4)	$674,051	$676,300	-$2,249	-0.3%	$688,238	-2.1%
Debt Service	$187,072	$188,315	-$1,243	-0.7%	$151,775	23.3%
Total Program Payments	**$12,301,005**	**$12,647,203**	**-$346,198**	**-2.7%**	**$12,100,131**	**1.7%**
TRANSFERS						
Local Govt Distribution	$0	$0	$0	---	$0	---
Budget Stabilization	$0	$0	$0	---	$0	---
Other Transfers Out	$30,975	$19,750	$11,225	56.8%	$15,988	93.7%
Total Transfers Out	$30,975	$19,750	$11,225	56.8%	$15,988	93.7%
TOTAL GRF USES	**$12,331,980**	**$12,666,953**	**-$334,973**	**-2.6%**	**$12,116,119**	**1.8%**

(1) Includes Primary, Secondary, and Other Education.
(2) Includes the Department of Job and Family Services, exclusive of Medicaid, TANF, and General/Disability Assistance.
(3) Includes Mental Health, Mental Retardation and Developmental Disabilities, and Other Human Services.
(4) Includes property tax rollbacks, homestead exemption, and tangible property tax exemption.

* August 2003 estimates of the Office of Budget and Management.

Detail may not sum to total due to rounding.

Health Care/Medicaid. In December, the Health Care/Medicaid program (primarily line item 600-525) posted a negative disbursement variance of $62.4 million; for the year to date, the variance is $104.6 million below estimate. As we see in Table 6, nearly half of the net December and year-to-date negative disbursement variances is the Inpatient Hospitals service category. Part of the variance in this service category, for both the month and the fiscal year, can be traced to the fact that mandated rate adjustments for children's hospitals have not yet been implemented. The Department of Job and Family Services (JFS) has indicated that when these adjustments are implemented, they will be retroactive. A significant portion of the negative disbursement variance in this service category (and in several other service categories) can be traced to lower than expected caseload growth and to an unusually low level of payments made in the final week of December, which appears to have resulted from the timing of payments.

Another notable negative disbursement variance is the All Other service category, which was under estimate by $16.5 million in December and stands at $44.3 million under estimate for the year to date. The negative variance in this service category seems to be tied to the timing of payments and to caseload growth lower than anticipated.

Table 6
Health Care Spending in FY 2004
Medicaid, ALI 600-525
($ in thousands)

	December				Year-to-Date Spending			
Service Category	**Actual**	**Estimate**	**Variance**	**Percent Variance**	**Actual thru Dec.**	**Estimate thru Dec.**	**Variance**	**Percent Variance**
Nursing Facilities	$205,942	$208,347	($2,405)	-1.2%	$1,292,220	$1,254,967	$37,253	3.0%
Payments	$215,965	$218,468	($2,503)	-1.1%	$1,351,590	$1,314,577	$37,014	2.8%
NF Franchise Fees Offset[1]	($10,023)	($10,121)	$98	-1.0%	($59,371)	($59,610)	$239	-0.4%
ICF/MR	$34,117	$34,876	($758)	-2.2%	$209,652	$210,623	($971)	-0.5%
Payments	$35,838	$36,639	($801)	-2.2%	$219,851	$220,965	($1,114)	-0.5%
ICF/MR Franchise Fees Offset	($1,720)	($1,763)	$42	-2.4%	($10,199)	($10,342)	$143	-1.4%
Inpatient Hospitals	$95,597	$125,460	($29,864)	-23.8%	$627,494	$679,857	($52,363)	-7.7%
Outpatient Hospitals	$47,121	$54,332	($7,211)	-13.3%	$282,295	$292,640	($10,345)	-3.5%
Physicians	$49,821	$54,266	($4,444)	-8.2%	$273,334	$291,223	($17,890)	-6.1%
Prescription Drugs	$168,463	$163,881	$4,583	2.8%	$851,045	$861,835	($10,790)	-1.3%
HMO	$73,874	$75,334	($1,460)	-1.9%	$504,088	$498,117	$5,971	1.2%
Medicare Buy-In	$11,848	$12,914	($1,067)	-8.3%	$75,018	$77,149	($2,130)	-2.8%
ODJFS Waiver[2]	$18,384	$20,690	($2,306)	-11.1%	$94,317	$107,545	($13,228)	-12.3%
All Other[3]	$69,609	$86,102	($16,493)	-19.2%	$406,135	$450,465	($44,331)	-9.8%
CHIP II[4]	$6,138	$6,037	$101	1.7%	$35,337	$32,475	$2,862	8.8%
DA Medical[5]	$7,541	$8,577	($1,037)	-12.1%	$47,034	$50,101	($3,068)	-6.1%
Total ALI 600-525	$788,455	$850,815	($62,360)	-7.3%	$4,697,968	$4,806,998	($109,030)	-2.3%
DSH Offset	$0	$0	$0		$0	$0	$0	
Drug Rebates	($42,005)	($41,978)	($27)		($167,504)	($169,081)	$1,577	
FY 2002 Encumbrance	$0	$0	$0		($71,000)	($39,781)	($31,219)	
Prior Period ALI 600-525	$0	$0	$0		$34,073	$0	($34,073)	
Total Health Care (Net of Offsets)	**$746,450**	**$808,837**	**($62,387)**	**-7.7%**	**$4,493,537**	**$4,598,136**	**($104,599)**	**-2.3%**
Est. Federal Share[6]	$438,134	$474,753	($36,618)		$2,637,513	$2,698,908	($61,395)	
Est. State Share	$308,316	$334,084	($25,769)		$1,856,024	$1,899,228	($43,204)	

1. Some of the money generated from nursing home franchise permit fees is used to make payments to nursing facilities to offset GRF nursing facilities spending. The NF franchise fee is $3.30 per bed per day in FY 2002 and is $4.30 per bed per day for FYs 2003 through 2005.
2. Waivers provide home-care alternatives to consumers whose medical conditions/functional abilities would otherwise require long-term care facility residence.
3. "All Other" includes all other health services funded by line item 600-525.
4. CHIP II provides health care coverage for children under age 19 whose family incomes are between 150% and 200% of FPL. The state receives enhanced FMAP for CHIP II.
5. DA Medical is a state-only funded program.
6. The federal madical assistance percentage (FMAP) used in this table is a blended rate of 58.70%.

Note: Due to accounting differences, the totals do not exactly match the amounts from Tables 4 and 5.

Source: BOMC8300-R001, BOMC8350-R001&R002 Reports, Ohio Department of Job & Family Services.

Table 7
FY 2004 to FY 2003 Comparison of Year-to-Date Health Care Spending
($ in thousands)

Service Category	FY 2004 Yr.-to-Date as of Dec. '03	FY 2003 Yr.-to-Date as of Dec. '02	Dollar Change	Percent Increase
Nursing Facilities	$1,292,219,658	$1,226,672,639	$65,547,019	5.34%
Payments	$1,351,590,227	$1,282,975,582	$68,614,645	5.35%
NF Franchise Fees Offset[1]	($59,370,569)	($56,302,943)	($3,067,626)	5.45%
ICF/MR	$209,652,064	$204,475,831	$5,176,233	2.53%
Payments	$219,851,077	$214,758,074	$5,093,003	2.37%
ICF/MR Franchise Fees Offset)	($10,199,013)	($10,282,243)	$83,230	-0.81%
Inpatient Hospitals	$627,494,396	$648,924,065	($21,429,669)	-3.30%
Outpatient Hospitals	$282,294,653	$274,822,270	$7,472,383	2.72%
Physicians	$273,333,685	$262,038,314	$11,295,371	4.31%
Prescription Drugs	$851,044,817	$766,552,658	$84,492,159	11.02%
HMO	$504,088,257	$340,929,492	$163,158,765	47.86%
Medicare Buy-In	$75,018,252	$70,864,149	$4,154,103	5.86%
ODJFS Waiver[2]	$94,317,136	$89,102,293	$5,214,843	5.85%
All Other[3]	$406,134,587	$382,383,626	$23,750,961	6.21%
CHIP II[4]	$35,337,157	$28,434,967	$6,902,190	24.27%
DA Medical[5]	$47,033,576	$47,657,760	($624,184)	-1.31%
Total Health Care	**$4,697,968,238**	**$4,342,858,064**	**$355,110,174**	**8.18%**
DSH Offset	$0	($89,036,668)	$89,036,668	
Drug Rebates	($167,504,030)	($121,881,308)	($45,622,722)	
Prior Year Encumbrance	($71,000,000)	($83,538,675)	$12,538,675	
Prior Period ALI 600-525	$34,072,774	$84,634,584		
Total Health Care (Net of Offsets)	**$4,493,536,982**	**$4,133,035,997**	**$360,500,985**	**8.72%**
Est. Federal Share[6]	$2,637,512,965	$2,425,914,390	$211,598,575	
Est. State Share	$1,856,024,017	$1,707,121,607	$148,902,410	

1. Some of the money generated from nursing home franchise permit fees is used to make payments to nursing facilities to offset GRF nursing facilities spending. The NF franchise fee is $3.30 per bed per day in FY 2002 and is $4.30 per bed per day for FYs 2003 through 2005.
2. Waivers provide home-care alternatives to consumers whose medical conditions/functional abilities would otherwise require long-term care facility residence.
3. "All Other" includes all other health services funded by line item 600-525.
4. CHIP II provides health care coverage for children under age 19 whose family incomes are between 150% and 200% of FPL. The state receives enhanced FMAP for CHIP II.
5. DA Medical is a state-only funded program.
6. The federal madical assistance percentage (FMAP) used in this table is a blended rate of 58.70%.

Source: BOMC8300-R001, BOMC8350-R001&R002 Reports, Ohio Department of Job & Family Services.

Also significantly under estimate is the Physicians category ($17.9 million under estimate for the year to date). This can be explained in part by a higher than projected growth in managed care enrollment, and thus lower than anticipated growth in the alternative Physicians category.

Partially offsetting these negative disbursement variances is the Nursing Facilities service category, which is over the year-to-date estimate by $37.3 million. The Department of Job and Family Services reports that "bed days" in nursing facilities are higher than expected, while per diems for Nursing Facilities have behaved as expected.

As noted in Table 7, the HMO category has posted a year-over-year growth rate of 47.9% so far this fiscal year. While HMO enrollment has been higher than expected (and this is reflected in the $6.0 million positive year-to-date variance noted in Table 6), what explains the bulk of this large growth rate is the fact that some HMO payments from June were delayed at the request of the Office of Budget and Management (OBM) so that they would be made in the new fiscal year. In addition, the first quarter of FY 2004 had 14 weeks in it, rather than the regular 13 weeks.

The estimated total number of Medicaid eligibles in December 2003 was 1,646,557, an increase of nearly 50,000, or 3.1%, since June 2003. The number of Covered Families and Children (CFC) eligibles stands at about 1,230,000, while the number of Aged, Blind, and Disabled (ABD) eligibles is now slightly over 410,000. The number of ABD eligibles is below what was forecast for this point in the fiscal year by about 7,000, and the number of CFC eligibles is over the forecast by about 1,000. Although greatly outnumbered by the CFC population, the ABD population accounts for over 70% of all Medicaid expenditures.

Under the federal Jobs and Growth Tax Relief Reconciliation Act of 2003 (H.R. 2), passed by Congress in May 2003, the federal government is providing temporary fiscal relief to the states in the amount of $20 billion. The states are to receive $10 billion in flexible assistance for essential government services or federal mandates, and $10 billion in the form of a 2.95% increase in the federal matching assistance percentage (FMAP) rate for Medicaid services. Ohio's share of these funds is $384.0 million in flexible assistance and $386.1 million in estimated increased federal Medicaid reimbursements. Ohio has received its $384.0 million in flexible assistance funds, and these have been deposited into the GRF.

The additional revenue from the increase in the FMAP is based on Medicaid reimbursements for services provided from April 1, 2003 to June 30, 2004. In accordance with Section 145 of H.B. 95 of the 125th General Assembly (the general operating appropriations act), the additional revenue is to be deposited into the newly created Federal Fiscal Relief Fund (Fund FY9). As of January 12, 2004, Ohio has received $216.9 million in additional revenue because of the increased FMAP, which is about 56% of the estimated $386.1 million, and these funds have been deposited into Fund FY9. Out of Fund FY9, the Director of Budget and Management will transfer $18,611,156 toward the end of FY 2004 and $90,851,972 in FY 2005 to the newly created Medicaid Reserve Fund (Fund FY8). The money in the Medicaid Reserve Fund will be used to purchase Medicaid services and draw down additional federal funds. Any funds in Fund FY9 that are not transferred to Fund FY8 are to be deposited into the GRF.

Job and Family Services. Through the end of December, disbursements for the Department of Job and Family Services operating and subsidy programs now stand at $40.7 million under the estimate for the year to date. These disbursements are captured in the Other Welfare subcategory in Tables 4 and 5, which excludes the separately tracked Medicaid, TANF, and Disability Assistance programs.

Little has changed in this subcategory since last month's report. Line item 600-416, Computer Projects, accounted for $15.4 million of this negative year-to-date disbursement variance. While about a third of this variance can be traced to slower than anticipated billing and payments, it appears that the remainder of this variance stems from prior-year appropriations to this line that will go unused and lapse to the GRF. Another $11.1 million of the negative year-to-date disbursement variance can be traced to line item 600-321, Support Services; a large portion of this ($5.4 million) stems from a planned purchase of office furniture that is being made by Ohio Penal Industries. There was some delay in the delivery of this furniture, but it is now slowly being delivered and installed. The Department has received approval from OBM to extend the encumbrance of these funds until the end of FY 2004. The remainder of the negative variance in line item 600-321 can be traced to slower than anticipated reorganization of the Department's "central campus."

TANF. In December, the Temporary Assistance for Needy Families (TANF) program posted a negative disbursement variance of $12.7 million to put the program below estimate for the year to date by a net of $11.0 million. This negative disbursement variance can be traced largely to line item 600-413, Child Care Match/MOE, which is under estimate for the year to date by $14.4 million.

So far this fiscal year, utilization of child care has been lower than anticipated by the estimates. If the caseload does not take up this slack as the fiscal year winds down, the Department reports that it will begin using the remaining balance to fund nonguaranteed cases to meet the state's maintenance of effort (MOE) requirement. December disbursements from line item 600-410, TANF State, were also under estimate by $4.5 million. This was primarily due to lower than anticipated advances to counties.

At the end of December, the number of TANF recipients was about 197,000, and the number of assistance groups (cases) was nearly 88,000. This is about 1,000 fewer recipients than one year ago but about 700 more assistance groups. This circumstance of a smaller ratio of recipients to assistance groups is part of a long-term trend in the TANF caseload. The average TANF assistance group now has 2.2 members, whereas in the early 1990s the average assistance group was at one point composed of 2.9 members. The reduction in the average size of assistance groups is connected to the greater share of the caseload composed of "child only" assistance groups, which are now 48% of the total number of assistance groups.

MR/DD. At the end of December, the Department of Mental Retardation and Developmental Disabilities posted a $9.1 million year-to-date negative disbursement variance, down by $11.3 million from the November figure. This variance, as we have noted in previous months, stems largely from two factors. One factor is the timing of Medicaid payments to providers. The second factor is the slower than anticipated process of distributing Medicaid funds to the counties, which impacted several line items. The largest contributor to the negative year-to-date variance was line item 322-417, Supported Living, which is now under estimate by $8.5 million.

Mental Health. In December, the Department of Mental Health did some catching up by posting a positive disbursement variance of $15.8 million, thus reducing the Department's negative year-to-date disbursement variance to $2.2 million. This catching up was registered primarily through a $13.9 million positive disbursement variance in line item 334-408, Community and Hospital Mental Health Services, and is largely due to the timing of local boards' requests for funds
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Education (-$85.4 million)

In December, the Education category posted a positive disbursement variance of $4.0 million, reducing the negative year-to-date variance to $85.4 million. The Department of Education accounted for $70.1 million, and the Board of Regents for $11.8 million, of the category's negative disbursement variance.

Department of Education. With a positive disbursement variance of $7.1 million in December, the Department of Education's disbursements for the year to date now stand at $70.1 below estimate. As is typical for the Department, timing was again largely responsible for the individual variances that produced the result for this month, with a good part of December's positive disbursement variance compensating for negative variances in earlier months.

Through December, the three largest contributors to the negative year-to-date disbursement variance in the Department were line item 200-426, Ohio Education Computer Network ($12.2 million under estimate), line item 200-503, Bus Purchase Allowances ($11.4 million under estimate), and line item 200-433, Reading/Writing/Math Improvement ($9.8 million under estimate). Line item 200-426, Ohio Education Computer Network, is used to maintain and provide technical assistance for a system of information technology throughout Ohio. The bulk of this line item is used to support connecting public and state-chartered nonpublic schools to the state's education network, to each other, and to the Internet. This activity just seems to be taking longer than was anticipated. Disbursements from line item 200-503 should catch up to the estimate as a result of a January approval by the Controlling Board to release funds for these allowances. And the variance in disbursement activity from line item 200-433 appears to have resulted merely from the timing of payment processing.

Regents. In December, the Board of Regents posted a negative disbursement variance of $5.9 million, thus increasing its year-to-date negative variance to $11.8 million. Missed December payments from line items 235-531, Student Choice Grants, and 235-549, Part-time Student Instructional Grants, produced negative variances of $17.9 million and $5.5 million, respectively. These missed payments were the result of late reporting from some campuses. A positive disbursement variance for the month in the amount of $11.2 million in line item 235-503, Ohio Instructional Grants, was partially offsetting.

Government Operations (-$80.8 million)

For the year to date, disbursement activity in the Government Operations category stands at $80.8 million under the estimate. The Department of Rehabilitation and Correction contributed $42.7 million of that figure. The Department of Youth Services (DYS) disbursements were under estimate in December, increasing its year-to-date negative variance to $17.2 million. The bulk of DYS's disbursement variance is traceable to changes in the pattern of disbursements required by the operating budget. Those changes were not reflected in the estimates. Disbursement activity in the Department of Rehabilitation and Correction will be discussed in more detail below.

A noteworthy positive disbursement variance occurred in the Department of Public Safety when the Department paid $6.0 million in state matching funds to the Federal Emergency Management Agency for different grants for disasters that the state had received. This payment had not been included in the estimates, thus producing a significant disbursement variance for the Department.

Rehabilitation & Correction. The disbursement picture in the Department of Rehabilitation and Correction is much the same as last month, although a December negative disbursement variance of $2.6 million increased the negative year-to-date disbursement variance to $42.7 million.

As we have reported for the last few months, the Department's year-to-date negative disbursement variance is traceable primarily to line item 501-321, Institutional Operations, which reflects current shortages in staff primarily in the northern part of the state. When the Lima Correctional Institution closed in July of 2003, some staff positions were eliminated while other positions, particularly corrections officers, were to be moved to other northern institutions and paid for with funds saved from the closing. The estimates for this line item anticipated that part of the funding for staff that was freed up by the closing would be used elsewhere in the system. Since this closure is in litigation and the institution remains partially in operation, many of these other positions remain vacant. In addition, the Department has delayed some equipment purchases from line item 501-321 until later in the fiscal year to ensure that there are sufficient funds.

Tax Relief (-$2.2 million)

The Property Tax Relief program, which carries an FY 2004 GRF appropriation of over $1.3 billion, reimburses school districts and local government for revenue that is lost due to tax relief provided by state law to property owners and businesses through the homestead exemption, the property tax rollbacks, and the $10,000 tangible tax exemption programs. Tax relief funds are disbursed to school districts and local governments by the Department of Education and the Department of Taxation, respectively. Each of these departments divides its property tax relief program into two components: real property tax credits/exemptions, and tangible tax exemptions. Total payments in the program were $82.4 million over the estimate for December.

This reduced the negative disbursement variance in the program to $2.2 million for the year to date. Disbursement variances in the tax relief program are usually traceable to the timing of when county auditors submit requests for reimbursement.

**LSC colleagues who contributed to the development of this disbursement report included, in alphabetical order, Sara Anderson, Melaney Carter, Ivy Chen, Phil Cummins, Erin Jones, Chris Murray, Laura Potts, David Price, Joseph Rogers, Maria Seaman, Clay Weidner, and Holly Wilson.*

Lottery Profits Quarterly Report

Lottery Ticket Sales and Profits Transfers, Second Quarter, Fiscal Year 2004

— *Jean Botomogno*

Ticket Sales

In the second quarter of FY 2004, total Ohio Lottery ticket sales were $549.8 million, $54.2 million or 10.9% higher than ticket sales in the first quarter. Higher total ticket sales in the second quarter were due to an increase of $58.7 million (22.9%) in Instant ticket sales. Instant tickets sales were $314.6 million, $79.4 million (33.8%) higher than on-line ticket sales[1] in the second quarter. Instant ticket sales are historically highest in the second quarter due to the large number of seasonal Instant games offered by the Ohio Lottery. On-line ticket sales were $235.2 million, $4.5 million or 1.9% lower than sales in the first quarter. Relatively low Super Lotto and Mega Millions jackpots hurt on-line sales in October and November 2003. Mega Millions' roll in December, which ended with an Ohio winner in January of a $162 million jackpot, made up for low sales of this game earlier in the quarter. Table 1 compares first- and second-quarter sales per game in FY 2004. Among on-line games, ticket sales increased for Pick 4 ($1.6 million or 4.0%) and Mega Millions ($1.1 million or 2.7%). At $16.5 million, second-quarter Buckeye 5 sales were similar to sales in the first quarter. Sales of the remaining on-line games declined. Super Lotto sales were down $4.4 million or 11.3%. Pick 3 sales declined 2.3 million or 2.4%.

Compared to second-quarter results a year ago in FY 2003, total ticket sales were up $11.4 million or 2.1% in the second quarter of FY 2004. Instant sales were up $17.7 million or 6.0%. On-line ticket sales declined $6.3 million or 2.6%. Most of the decline was directly related to a decrease of $5.8 million (14.3%) in Super Lotto sales. Kicker sales, which are correlated with Super Lotto sales, declined $0.8 million or 11.5%. Pick 3 sales were down $5.6 million or 5.6%. Buckeye 5 sales fell $0.4 million or 2.6%. Among on-line games, Pick 4 and Mega Millions sales increased $1.6 million (4.0%) and 4.8 million (13.2%), respectively.

Midyear Summary

Table 2 summarizes midyear ticket sales by game and compares ticket sales in FY 2004 and in the previous fiscal year. As of December 2003, year-to-date ticket sales in FY 2004 were $1,045.4 million. Compared to the same

Table 1: Quarterly Lottery Ticket Sales by Games in FY 2004, in millions of dollars

	Pick 3	Pick 4	Kicker	Buckeye 5	Super Lotto	Mega Millions	Instant	On-line	Total
Q1	$98.2	$39.1	$6.5	$16.5	$39.4	$40.0	$255.9	$239.7	$495.6
Q2	$95.9	$40.6	$6.1	$16.5	$35.0	$41.1	$314.6	$235.2	$549.8
$ Change	-$2.3	$1.6	-$0.4	$0.0	-$4.4	$1.1	$58.7	-$4.5	$54.2
% Change	-2.4%	4.0%	-6.1%	0.0%	-11.3%	2.7%	22.9%	-1.9%	10.9%

Totals may not add up due to rounding.

Table 2: Midyear Ticket Sales by Games in FY 2004 and FY 2003, in millions of dollars									
Year	Pick 3	Pick 4	Kicker	Buckeye 5	Super Lotto	Mega Millions	Instant	On-line	Total
FY 2004	$194.1	$79.7	$12.6	$33.0	$74.4	$81.1	$570.5	$474.9	$1,045.4
FY 2003	$200.2	$76.5	$13.8	$34.3	$80.9	$90.3	$535.5	$496.0	$1,031.5
$ Change	-$6.1	$3.2	-$1.2	-$1.3	-$6.5	-$9.2	$35.1	-$21.1	$13.9
% Change	-3.0%	4.2%	-9.0%	-3.8%	-8.0%	-10.2%	6.5%	-4.3%	1.3%

Totals may not add up due to rounding.

period a year ago, first-half sales increased $13.9 million (1.3%), with Instant sales more than erasing the decline in sales of on-line games. Instant sales improved $35.1 million (6.5%) whereas on-line sales declined $21.1 million (4.3%). Compared to sales in FY 2003, only Pick 4 had higher sales in the first half of FY 2004. Pick 3 sales decreased $6.1 million (3.0%). Kicker sales were down $1.2 million (9.0%). Super Lotto sales fell $6.5 million (8.0%). Buckeye 5 sales declined $1.3 million (3.8%), and Mega Millions sales shrunk $9.2 million (10.2%).

Comparing on-line and Instant games, Instant ticket sales were $95.6 million (20.1%) higher than on-line sales as of December 31, 2003. In the same period in FY 2003, Instant ticket sales were $39.5 million (7.9%) ahead of on-line sales. The ratio of Instant to total ticket sales increased to 54.6% in the first half of FY 2004, up from 51.9% in the same period in FY 2003. The payout ratio for Instant games was about 66% in FY 2003 while that of on-line games was 51%. For an extra dollar of ticket sales, 66 cents is returned to players who purchase Instant tickets compared to 51 cents paid out for the purchase of on-line games. Thus, the increase in ticket sales is somewhat mitigated by a decrease in the overall profitability of sales.

Transfers to LPEF

Table 3 summarizes transfers from operations to the Lottery Profits Education Fund (LPEF). Transfers in the second quarter of FY 2004 were $166.4 million, up from $152.2 million in the first quarter. The Ohio Lottery had anticipated transfers of $154.7 million in the first quarter and $166.0 million in the second quarter. Although transfers were higher by $14.2 million compared to the first quarter, second-quarter transfers were just $0.4 million above projected transfers for the quarter. As of December 2003, year-to-date transfers in the current fiscal year were $2.1 million below projected transfers. Transfers were above 30% of ticket sales in each quarter.

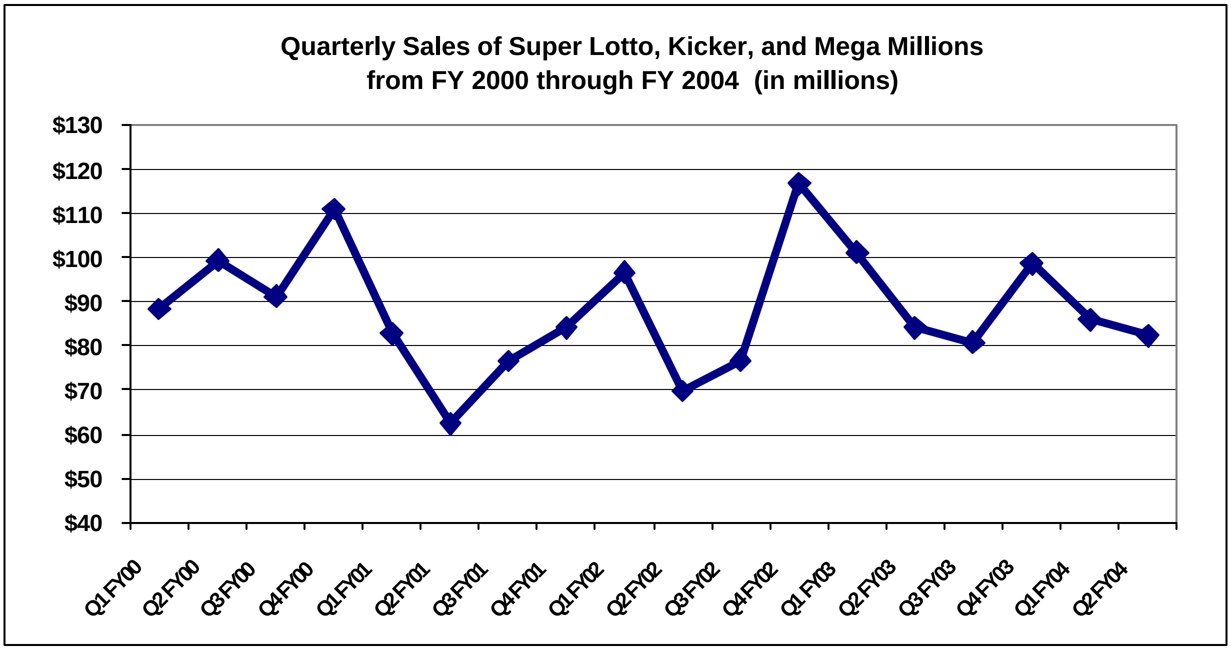
As of December 2003, year-to-date transfers were $318.6 million, $13 million or 4.2% more than transfers in the same period last year. The variance between actual and projected transfers was $2.1 million, $6.1 million less than the variance recorded at the end of December 2002.

Super Lotto (and Kicker) Sales Still Outpacing Mega Millions Ticket Sales

The Ohio Lottery joined Mega Millions on May 15, 2002 (fourth quarter of FY 2002). Super Lotto ticket sales were expected to

Table 3: Quarterly Lottery Ticket Sales and Transfers to LPEF in FY 2004, in millions of dollars						
Quarter	Tickets Sales	Actual Transfers	Projected Transfers	Dollars Variance	% Variance	Transfers as a % of Sales
Q1	$495.6	$152.2	$154.7	-$2.5	-1.6%	30.7%
Q2	$549.8	$166.4	$166.0	$0.4	0.3%	30.3%
$ Change	$54.2	$14.2	$11.3	N/A	N/A	N/A
% Change	9.9%	8.6%	6.8%	N/A	N/A	N/A

Totals may not add up due to rounding.



decline because its top prize would become less exciting to players, and some players would substitute Mega Millions tickets for Super Lotto tickets. The loss in Super Lotto sales would be more than compensated by ticket sales of Mega Millions, and the new game would improve the overall profitability of on-line games. Total combined sales of Super Lotto, Kicker, and Mega Millions were $389.5 million in FY 2000, $305.4 million in FY 2001, $359.6 million in FY 2002, and $364.3 million in FY 2003. Thus, the addition of Mega Millions to the on-line games appears to have achieved the goal of increasing ticket sales. The graph above illustrates quarterly expenditures on tickets for Super Lotto, Kicker, and Mega Millions, from the first quarter of FY 2000, through the second quarter of FY 2004. During this period, combined Super Lotto and Kicker sales were the lowest ($62.3 million) in the second quarter of FY 2001, and aggregate Mega Millions, Super Lotto, and Kicker sales were the highest ($116.6 million) in the fourth quarter of FY 2002.

Table 4 compares quarterly ticket sales of Mega Millions and Super Lotto and Kicker in FY 2003 and in FY 2004 (as of December 2003). The last quarter of FY 2002 was excluded because Mega Millions started midway in that quarter.

Table 4 shows that, except in the first quarter, FY 2003 Mega Millions sales were generally lower than Super Lotto sales. Fiscal Year 2004 Mega Millions sales were $6.0 million less than Super Lotto and Kicker sales in the first quarter and barely edged out the other games in the second quarter. Total Mega Millions sales were $17.9 million less than Super Lotto and Kicker sales in FY 2003 and FY 2004, or $3.0 million per quarter. The gross profit margin for Mega Millions over the six quarters was about 52.5% of sales. Gross profit margins for Super Lotto and Kicker were 37.6% and 62.6%, respectively. The weighted average of these margins was approximately 39.9%, about 12.6 points less than that of Mega Millions. This implies that the lower level of sales of Mega Millions (relative to sales of Super Lotto/Kicker) reduced the gross profit from these three games by an average of about $380,000 per quarter from the first quarter of FY 2003 through the second quarter of FY 2004.

Texas Joins Mega Millions

The Texas Lottery became the 11th U.S. jurisdiction to launch Mega Millions when tickets went on sale December 3, 2003, joining Georgia, Virginia, Illinois, Maryland, Massachusetts, Michigan, New Jersey, New York, Ohio, and Washington. In addition, the

Table 4: Quarterly Mega Millions, Super Lotto, and Kicker sales in FY 2003 and FY 2004 (in millions)							
Games	FY03Q1	FY03Q2	FY03Q3	FY03Q4	FY04Q1	FY04Q2	Total
Super Lotto & Kicker	$47.0	$47.7	$43.5	$49.9	$46.0	$41.0	$234.2
Mega Millions	$54.0	$36.3	$37.2	$48.7	$40.0	$41.1	$216.3
Variance	$7.0	($11.4)	($6.3)	($1.2)	($6.0)	$0.1	($17.9)

Totals may not add up due to rounding.

Texas Lottery is pioneering an add-on game called the "Megaplier." A Megaplier number of 2, 3, or 4 is randomly selected for each Mega Millions drawings. For an extra $1, Texas players have the option to double, triple, or quadruple their winnings (except for the grand prize). For example, if the Megaplier number selected is 3, a $2 prize for matching the Mega Ball would become $6, and a prize worth $175,000 for matching 5 numbers, but not the Mega Ball, would be worth $525,000 for those who purchased the Megaplier feature. The Texas Lottery is estimating annual sales of about $390 million per year for Mega Millions and $62 million for Megaplier. Per capita sales would be $17.60 for Mega Millions. As a comparison, Ohio Mega Millions per capita sales were about $15.50 in FY 2003. With the addition of Texas, the jackpot may increase more rapidly when there are no winners and potentially generate more ticket sales in Ohio.

[1] On-line games refer to Pick 4, Pick 3, Kicker, Buckeye 5, Super Lotto, and Mega Millions. These games are played via a terminal at a Lottery sales agent. Those terminals are linked to Ohio Lottery headquarters computers. On-line games do not refer to "Internet" lottery sales; such games are not run by the Ohio Lottery.